THE HONORABLE MARSHA J. PECHMAN

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

COSTCO WHOLESALE CORPORATION, a Washington corporation, Plaintiff, v. ROGER HOEN, VERA ING, and MERRITT LONG, in their official capacities as members of the Washington State Liquor Control Board, Defendants, and WASHINGTON BEER AND WINE WHOLESALERS ASSOCIATION, a Washington non-profit corporation, Intervenor Defendant.	NO. CV04-0360P **COSTCO'S SUMMARY OF DEPOSITION DESIGNATIONS**

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SUMMARY OF DEPOSITION DESIGNATIONS

Janice Lee Britt, current LCB employee and former MIW Division Supervisor

Restraints are not applied or supervised with the purpose of affecting consumption.

- The beer price posting time period was based on industry's request. 15:21-16:15.
- The LCB conducted a survey of the industry to determine how many days a price hold should remain in effect and did not seek input on less than 30 days. 53:10-55:11.
- Price postings allow for self-monitoring, meaning that suppliers and distributors can freely check (effective) price postings of their competitors. 48:15-49:7
- Changes to the price posting regulations have all been in response to requests from the industry. 49:12-24.

Lester Dalrymple, long-time LCB employee in licensing and enforcement divisions

1. The restraints are not necessary to promote temperance or efficient tax collection.
   - Retailers are prohibited from centrally warehousing wine and beer only because warehousing is considered a distributor function. 22:19-25; 25:6-14.
   - A distributor's warehouse need not have a security alarm or a 24-hour or any other guard. It must only be large enough to handle the anticipated business and be in compliance with general health, building, and zoning codes. 32:10-34:16.
2. Restraints are not applied or supervised with the purpose of affecting consumption.
   - In 1993, the LCB was only reviewing a random 20% sample of price postings each month. 48:1-49:5.
   - The LCB did not check whether closeouts of a product had been completed in the required six month time frame. 53:7-54:11.
   - The LCB did not track price increases based on the price posting data. 54:19-21.
   - The LCB never studied how price posting, quantity discounts, the minimum price requirement or any of the other restraints affected alcohol consumption. 85:10-86:11.

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- Prior to and for a short period after price posting became automated, Paul Crampton and his wife generated monthly reports that collected all of the distributor price postings and sent them to WBWWA members. 61:3-14.

3. The State cannot prove that alternatives to the restraints would be ineffective.

   - The LCB has never analyzed whether or not it would make sense to allow retailers to warehouse wine and beer, proposed such an analysis or discussed whether the central warehousing ban was a good or bad policy. 24:9-5.
   - The LCB considered eliminating the price posting system once. WBWWA strongly opposed it, and the idea was dropped. The only nongovernmental individuals present at the meeting at which this topic was discussed were individuals representing WBWWA. 62:10-18; 63:9-20; 67:14-70:9.

Heidi Ensign, LCB Non-Retail Compliance Administrator

1. Price posting is unnecessary to ensure enforcement of retail-level controls on abusive consumption or efficient tax collection.

   - "As a matter of course," the LCB does nothing with the information from the time a supplier posts prices on the 25th of a month until the first day of the second month after that. 16:20-18:1.
   - The LCB only reviews the 10% mark-up when a distributor calls in trying to make a posting, not because someone has complained about the price. 19:9-21.
   - The LCB reviews a distributor's price posting or their mark-up for reasonableness. 87:6-14. The LCB only reviews the price posting at all when a concern is called in by someone from the outside. 21:18-22:7
   - Subjobbers, a distributor who sells to other distributors, are not required to post prices with a 10% mark-up. 28:1-6.
   - Suppliers and authorized representatives are not required to post "acquisition costs," thus the 10% mark-up requirement does not apply to manufacturers and authorized representatives. 34:4-36:2.

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- The LCB does nothing to monitor whether manufacturers are posting prices or selling at prices at least 10% above their cost of production. 38:3-8.
- The LCB does nothing to monitor whether in-state importers are posting prices 10% above acquisition cost. 39:14-23.

2. The restraints are not consistently applied.

- Manufacturers may grant purchase allowances, completion allowances and percentage depletion allowances to distributors. No such allowances are permitted between distributor and retailer. 39:24-42:6.
- Manufacturers may grant freight differentials to distributors, but retailers may not receive freight differentials from distributors. 42:11-18.

3. The minimum mark-ups are not reviewed by LCB.

- Ms. Ensign has never studied distributor mark-up levels. 43:3-5.
- The LCB does not review nor is it concerned with distributor mark-ups and how high they may be, nor has the LCB hired an economist to look at such issues. 43:6-45:2.

4. The LCB is not concerned with whether the restraints subsidize some retailers. 50:22-51:4.

5. Restraints are not applied or supervised with the purpose of affecting consumption.

- Before the lawsuit, the LCB did not concern itself with capturing data relating to distributor attempts to post at a price under the 10% minimum mark-up. 60:4-61:2.
- The LCB does not investigate whether distributors are selling below the 10% minimum, even after receiving an error message indicating that the distributor tried to post a price that was less than the mandatory 10% minimum mark-up. 61:9-62:6.
- The LCB does not distribute violation notices for failure to price a post above the mandatory 10% mark-up. 68:2-11.
- The LCB has no way to determine whether a manufacturer is posting above the 10% minimum mark-up. 70:23-71:5.

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6. Price postings are rejected due to form, not for the purpose of affecting consumption. The LCB rejects requests for late price postings when there is no good cause shown, without regard to the proposed price. 74-7:75:12; 76:21-24; 77:24-78:8; 79:6-9; 80:3-12; 86:23-87:2.

Jeffrey A. Hooker, former Costco buyer in Washington and California

1. The restraints produce inefficiencies, are unnecessary, and hurt consumers.

- The restraints prohibit efficiencies of scale by prohibiting quantity discounts. 12:14-13:4.
- Costco's economic model is based on the theory that if you are able to be more competitive and buy in volume, there should be a value attributed to that efficiency. 13:14-16.
- Costco strives to create efficiencies so as to create value for and reward its members. This serves as a means to differentiate Costco from other retailers and provide consumers a reason to continue to shop at Costco. 16:3-17:7.
- Costco's prohibition from realizing value as a result of its efficiencies inhibits Costco from providing additional value to its members. 13:22-25.
- California's alcohol regulatory system, as opposed to Washington's, rewards efficiencies of suppliers, manufacturers and retailers, which results in consumers being rewarded with better value. 14:5-17.
- Costco does not have real choice in establishing what it will pay for beer and wine products; the pricing comes to Costco from the distributor and supplier. 25:17-24. Costco generally applies a mark-up of approximately 5-6.5% to beer. 24:16-25:5.
- The inability to buy wine direct from out-of-state wineries for Washington stores, as opposed to California stores, results in significant price differences between California and Washington for similar wines. 92:16-93:3.
- Almost across the board, after factoring out tax and freight, the cost to Costco for wine in Washington is higher than in California. The reasons for this are Washington's ban on volume discounts, central warehousing, credit terms, and the requirement of delivered pricing. 100:18-101:21.

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2. The restraints stabilize prices.

- The prices charged to Costco for a six-pack of Miller, Coors, and Budweiser were stable, with only two or three changes a year. 90:21-91:1.
- For 12 and 18-packs of beer, posted price "discounts" would rotate among Miller, Coors, and Budweiser almost every month. 91:3-6.

3. The State's actions are inconsistent with a goal of reducing beer and wine consumption.

- In many instances, the State liquor stores have sold beer and wine below Costco's acquisition cost. 126:24-127:7.
- This is a major disadvantage to Costco and other retailers who cannot meet the prices of the State liquor stores, which are competitors of private retailers. 128:4-12; 128:25-129:8.

4. Distributors provide services to other retailers that Costco does not receive, yet Costco must pay the same price as those retailers. 134:8-135:5; 135:18-25; 136:10-13.

5. Restraints are not necessary to ensure compliance with laws regarding selling to minors or intoxicated individuals. 137:14-21; 138:6-15; 139:1-6, 11-19.

Vera Ing, LCB Member and defendant

1. Restraints are not applied or supervised with the purpose of affecting consumption.

- After this lawsuit was filed, the LCB never publicly reviewed the challenged restraints to see if they were consistent with its missions and goals. 12:25-13:4.
- Prior to this lawsuit being filed, the LCB never reviewed the challenged restraints to see if they were consistent with its missions and goals during Ing's tenure (since 1999). 13:5-15.
- The LCB had never reviewed in a public session during Ing's tenure whether the quantity discount ban is consistent with the LCB's mission and goals. 14:25-15:4.
- Since Ing became a member of the LCB, the LCB has never analyzed whether the 10% minimum mark-up is too high, too low, or just right. 41:22-25.

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- During Ing's tenure, the LCB has never studied whether there would be negative impacts if there were open competition in the wine and beer distribution industry in Washington. 45:7-10.
- The LCB does not monitor how high mark-ups on beer and wine rise and is not concerned with how high the mark-up is from the distributor to the retailer. 47:11-13.
- A distributor can post a price as high as it wants to as long as it is above the 10% minimum mark-up and there is no supervision by the LCB as to the reasonableness of that price. 48:25-49:8.

2. The LCB uses the volume discount ban to ensure an even playing field for all retailers. Ing does not identify temperance or tax collection as the purpose for the ban on volume discounts. 17:10-13.

3. There is no state policy to increase price to reduce consumption. 17:5-9.

   - The LCB has "no mandate to increase or eliminate or reduce consumption." 24:24-25.
   - It is acceptable to the LCB if the total amount of consumption increases without abusive consumption increasing. 25:12-16.
   - The LCB's "concern is not what the price is." 73:19.
   - The LCB is not concerned if a distributor cuts its price by 20% so long as the price remains above the 10% minimum mark-up. 73:13-22.
   - The LCB does not care what retail prices are to the consumer. 80:12-15.
   - As far as the LCB is concerned, a retailer can sell the poorest quality wine with the highest alcohol content for as cheap as it wants as long as the retailer does not sell below cost. 80:3-15.

4. The restraints are not necessary to ensure an orderly market.

   - The LCB defines orderly distribution as the separation of alcohol distribution into a three-tier system in order to prevent vertical integration. 42:9-19; 167:7-8.
   - During Vera Ing's tenure, the LCB has not analyzed whether vertical integration or tied houses are still a problem today. 44:2-8.

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- A state could still have orderly procedures without the challenged restraints. 168:1-4.
- The three-tier system is not the only means of control. 168:5-18.

5. The LCB is not concerned with the federal interest in competition.

- "Competition in a common marketplace is not [the LCB's] responsibility." 74:13-14.
- The LCB is not concerned with the impact of the challenged restraints on competition. 76:16-19.

6. The LCB has never studied whether collecting tax through the manufacturer or the retailers, as opposed to the distributor, would be more or less effective. 65:25-67:8.

7. The interests of the LCB and WBWWA are aligned.

- Ing met with both State and WBWWA attorneys on three separate occasions to prepare for her deposition. 168:19-169:13.
- WBWWA attorney Guadnola has "been very helpful" to the LCB. 169:23.
- In executive session, the LCB approved entry of the joint defense agreement with WBWWA because the LCB wanted share the cost of the litigation with WBWWA. 174:3-19; 175:1-7.

8. The State's actions are inconsistent with the alleged goal of reducing beer and wine consumption.

- The LCB's mission is to "maximize revenue to the state by operating efficient, convenient, and profitable retail stores." 182:1-7.
- The LCB is pursing efficiency at the State liquor stores because "[t]here's always room for improvement" and two governors have "emphasized performance-based operations." 185:12-18.
- The LCB is the leading agency that has emphasized performance-based operations at the State liquor stores. 185:18-19.

Merritt Long, LCB Chair and defendant

[Long deposition designations are included in summary of first week's testimony.]

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Carter Mitchell, former employee and Public Information Officer/Legislative Liaison

1. Price posting was added to statute due to the feeling that having it only in the WAC left it more susceptible to challenge. 17:12-18:1.

2. Restraints and policies serve private parties and other purposes, not reduction in abusive consumption.

- The LCB sought the input of the distributors when considering making the price posting system part of the statute. 22:3-7; 23:8-19.
- Changes to the bonded warehouse laws in 1995 had the purpose of making it simpler and more efficient for wineries to pick-up and deliver wine. 62:20-63:5. The LCB sought to have the Washington Wine Institute and WBWWA come together and work out a solution regarding bonded warehousing. 64:15-65:2.

3. The credit restraint was not considered necessary to promote temperance, an orderly market, or efficient tax collection. 76:15-77:5.

Roxie Studer-Eldred, LCB Information Technology Application Specialist

1. Burden of restraints falls on retailers, not suppliers or distributors.

- Prior to the price posting system going online, distributors and suppliers had to use the LCB's "trade room." The online system is limited to use by supplier and distributor licensees. Retailers still must travel to Olympia to the "trade room." 30:15-22; 34:19-35:9.

2. Restraints are not applied or supervised with the purpose of affecting consumption.

- Authorized representatives are not required to post "acquisition cost," therefore there is no way to measure the 10% mandatory mark-up. 44:12-45:1.
- Distributors can post prices at less than the 10% mark-up. 73:22-74:14.
- Manufacturers are not required to post production costs on the price posting system; therefore it is not possible for the system to identify whether or not the price posted is 10% above production cost. Thus, a manufacturer can post any price, above or below

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10% of its acquisition cost and the price posting system will accept it and there is no plan to change the system. 74:15-75:8; 90:3-13.

- Despite the law, the price posting system does not require self-distributing manufacturers to post prices that are 10% above production cost because production costs are not posted. 77:1-78:1.
- Despite the law, the price posting system does not require certificate of approval holders to post prices that are 10% above production cost because production costs are not posted. 78:2-17.
- Despite the law, the price posting system does not require out of state manufacturers to post prices that are 10% above production cost because production costs are not posted. 78:25-79:15; 79:25-80:22; 89:8-19.
- Despite the law, the price posting system does not require subjobbers to post prices that are 10% above production cost because acquisition costs are not posted. 81:7-82:3.

3. Manufacturers can post-off for a period of 30 days. If the post-off is not renewed, the last regular selling price will automatically resume without any input by the manufacturer. 51:11-25.

4. Price posting system is unnecessary for efficient tax collection.

- From 1997, when the price posting system went online, until at least 2005, the price posting system did not capture the tax paid by subjobbers. 57:12-58:11.
- Tax reporting is not done using the price posting system. There is a separate tax reporting program that is entered manually be the LCB after receiving emails or other hard-copy format from the distributors. 58:12-59:6.
- Missed tax reporting is not caught by the price posting system, but rather by audits. 60:5-25. There is no link between the tax reporting system and the price posting system. 61:5-15.
- Taxes are reported by the liter or by the barrel, not by item like the price posting system. 61;21-62:2.

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Heidi Whisman, LCB Director of Purchasing

1. The State's actions are inconsistent with the goal of reducing consumption.
   - The LCB's purchasing decisions do not consider the State's mandated ceiling of 35% net annual revenue. 20:18-21:13.
   - The Board considers the "marketability" of the product, not what the product can be bought or sold for. 22:19-23:12.
   - The Board's mark-up is considered and applied as one of many considerations in the decision to carry a particular wine including the need for certain categories of wine, how appealing the wine is to consumers and the value of the wine. 24:7-17; 25:10-13.
   - The State retail liquor stores offer discounts to consumers and deeper discounts to on-premises retailers. 28:11-25
   - The LCB retail stores, as dictated by the purchasing division, cut their prices on select wines during Washington Wine Month. 35:1-16.
   - The LCB retail stores give case-equivalent discounts. 36:16-25.
   - The LCB retail stores sell wine at lower prices than other retailers as evidenced by the Wine Strategy and the study conducted in connection with the Strategy. 43:3-6; 43:22-25 – 44:2

2. The restraints do not apply to the State.
   - The LCB retail stores are not precluded from asking for quantity discounts. 31:3-16.
   - The LCB retail stores are permitted depletion allowances while other retailers are not. 31:17-32:1.
   - The LCB does not post prices with the MIW section. 34:7-12.
   - The LCB has no obligation to hold its prices for 30 days. 34:13-18.
   - The LCB is permitted to centrally warehouse its product. 38:5-23.
   - The LCB receives products at a lower cost than do private retailers for the same products because shipments to the LCB do not have to go through the price posting process. 44:25-45:9; 45:17-46:8.

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3. Price posting is not necessary to ensure enforcement of retail-level controls on abusive consumption or efficient tax collection.

- Manufacturers are not required to file a cost of production, thus the LCB has no way to determine whether the manufacturer posts a price that is 10% above cost of production. 87:22-88:2; 90:24-91:11.
- The LCB does not review a distributor's price for reasonableness. 113:10-23.

4. Restraints mostly burden retailers.

- Other than it being the law, Ms. Whisman cannot explain why manufacturers may give allowances to distributors, but distributors may not pass those same allowances on to retailers. 107:13-18.

DATED: March 27, 2006.

s/ David J. Burman, WSBA # 10611
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Attorneys for Plaintiff Costco Wholesale Corporation

DECLARATION OF SERVICE

I declare that on March 28, 2006, I caused to be served upon counsel of record, listed below, via efiling or hand delivery, a true and correct copy of the foregoing Costco's Summary of Deposition Designations to the following:

David M. Hankins
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Attorney for Roger Hoen, Vera Ing, and Merritt Long

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Attorneys for Intervenor Defendant Washington Beer and Wine Wholesalers Association

I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED: March 28, 2006 at Seattle, Washington.

David J. Burman

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Qualifications

Exhibit TX ____ your CV?

offer

Education?

Area of expertise?

Teaching?

Key publications?

Consulting?

Worked for the State?

Other States?

Feds?

Only after decided to file case?

Have you previously studied Costco's business methods and those of other retailers?

Distributors?

[Analyzed wine and beer industries in particular?]

Preparation

Reviewed?

Testimony of defense experts and distributors?

TX 239 your report?

TX 241 your rebuttal report?

TX ___ the exhibits to your report.

offer

Reflect your opinions?

Offer Txs

Have you reviewed testimony of defense experts?

Assignment?

Analysis of competitive and efficiency impacts of WSLCB restraints on beer and wine distribution.

What restraints did you analyze?

Prepare a *CHART* reflecting those

Your conclusion?

Anticompetitive

Inefficient

No offsetting pro-competitive benefits.

Looking at each - Explain

Posting

Increases price transparency – aids in tacit collusion

Holding

Prevents efficient responses to unexpected demands

Promotes gluts and shortages

Does the "holding" restraint lead only to higher prices.

No.

Lower prices with high inventory levels

Higher prices with high demands e.g. favorable review

Minimum markups?

10% minimum generally not economically binding.

But circumstances of high inventories occur.

Uniform Pricing?

Anticompetitive –

single price easy to police with tacit collusion

no delivered prices, no volume discounts increase price transparency

Inefficient.

Buyers with capability to lower distribution costs can't take advantage.

Buyers have no incentive to develop lower cost methods of distribution.

No Credit?

Anticompetitive and inefficient.

What sort of retailers benefit from the prohibition

No Retailer Warehousing

Anticompetitive and inefficient

Retailer to retailer sales restraints?

Anticompetitive (absent uniform pricing)

Protects distributors from competition.

Inefficient

Prevents efficient retailer (e.g. lower warehousing and transportation costs) from passing on efficiencies.

Do the restraints increase all the prices paid by consumers?

No. Increase some (favored) lower others.

Explain.

Different cost to suppliers but same prices.

Price will be between.

Effective economic price discrimination.

Explain what you mean by "effective price discrimination?"

Price discrimination means charging different buyers prices that are in different relationships to costs.

Example.

If the pluses and minuses net out to no average price increase, does that mean no damage to competition?

By requiring that all buyers pay the same prices, do the restraints "level the playing field" for retailers?

> *To the contrary, the restraints "tilt" the playing field in favor of the higher cost retailers.*

Have you examined any evidence that the restraints in fact adversely impacted prices?

> *Two buck chuck.*
>
> *Exhibit B. TX___*
>
> *Exhibits C. TX___*

You have testified that the prices to some consumers will be higher and some will be lower, the defendants have stipulated that the average impact is to increase prices somewhat. Have you so concluded?

> *Stipulation.*
>
> *No theoretical or empirical support.*
>
> *Can you estimate an upper bound based on your analysis?*

If in fact the average price does increase as a result of the WSLCB retraints, will the consumption beer and wine in Washington decrease as a result?

> *Uncertain.*
>
> *Law of Demand not applicable.*
>
> > *Some higher and some lower prices.*
> >
> > *Increased availability.*
> >
> > *Increased promotions.*

Have you seen any analysis relevant to measuring the overall effect of the WSLCB restraints on consumption in Washington?

Does an average price increase imply that any particular group of wine and beer consumers will have lower consumption?

Consumers shopping at disfavored retailers lower consumption.

Consumers shopping at the favored retailers (convenience stores and on-site consumption) increased consumption.

Would economists assume that all wine and beer drinkers are the same?

Could such analysis be performed as to the characteristics of consumers that are likely to increase or to decrease consumption as a result of the restraints?

Yes. Identify the preferred shopping locations of consumer groups.

Are you aware of any such studies?

AIA EFFORTS?

By favoring smaller retailers will the restraints change the overall incentives for retailers to abide by rules controlling wine and sales and also to pay the state taxes?

Restraints increase the presence of the favored retailers.

Entrants become marginal sellers.

Larger disfavored sellers - sophisticated accounting systems, more to lose

Restraints shift sales from more compliant to less compliant retailers.

Do the restraints lead to "more orderly" marketing?

Not an economic term.

Casavant defined

Prices better match costs.

Control of gluts and shortages.

With definition – market handles, regulations foul up.

Is it generally accepted by economists that governmental restraints can reduce problems with gluts and shortages that might arise in a competitive market?

Is it generally accepted by economists that absent governmental restraints suppliers of wine and beer or similar products would tend to force retailers to engage in unlawful conduct in terms of retail sales?

Engage in promotional activities that they would not otherwise engage in?

Do the recent legislative changes allowing retailers to deal directly with manufacturers change the overall economic impact of the restraints?

In the direction of increasing competition.

Does not alter the overall anticompetitive impact of the restraints.

No warehousing.

No economies of scale in purchase through volume discounts.

No favorable credit opportunities.

How would an economist balance the damage to competition from the restraints against any beneficial impacts of reduced consumption?

Measure benefits.

Measure costs.

Done?

Costs – higher prices up to 5%.

Benefits – no evidence of desired reduction in consumption.

Are you aware of any such analysis that has been performed by the Legislature, WSLCB, or defense experts?